CHAPTER 3

Promoting exports—essential for transformation

The East (and South-East) Asian tiger economies used exports to power their economic transformation from the mid-1960s through the 1990s. Should Sub-Saharan countries try to do the same? Can they? And how?

Why export?

Exporting is critical for transforming small and medium-size economies. The opportunity to export widens the market available to domestic producers and thus increases potential demand and the prospects for higher prices. Higher demand allows a larger scale of production, which can increase employment and the use of other domestic factors of production. Larger scale production could also lower unit costs and increase competitiveness and thus boost profit margins for domestic producers. Exporting also enables a country to better align its production to its comparative advantage and to earn more from its factor endowments.

Exports also provide the foreign exchange to import the machinery and technology necessary in the short to medium term for technological upgrading. Over time, higher earnings from exports make it easier to finance investments (such as skills, technology development, and infrastructure) to change a country’s underlying factor endowments and comparative advantage. Exposed to competition on international markets, exporters have to increase their efficiency in production and marketing, in the process showing other domestic producers what is possible. Exporting also exposes domestic entrepreneurs to global tastes, standards, technologies, and best practices—providing opportunities for learning about new products, services, processes, and technologies that they could introduce at home.

Competition from imports on the domestic market also pressures domestic firms to be more efficient. Ultimately, however, the foreign exchange to pay for imports must come from exports. So, through all these channels, exporting can help the economy—particularly a small or medium-size one—to expand, raise employment and incomes, and promote structural change by facilitating learning and the introduction of new products, services, production processes, and technologies.

The East (and South-East) Asian tiger economies took advantage of such links to transform their economies from the mid-1960s through the 1990s.1 But that was decades ago. And the global economy has since changed. Can Sub-Saharan countries use the same export strategy today to drive their economic transformation? And how must they adapt that strategy to suit the times?
East Asian countries started with labor-intensive exports that took advantage of their relative abundance of labor and low wages. Before addressing these questions, consider some simple relationships between exports and GDP in the ACET 15 countries and in the comparator countries, six from East and South-East Asia. As a group the comparators attained higher growth than the ACET 15 did both in exports as a share of GDP and in real GDP per capita (figure 3.1). There clearly is a positive correlation between exports as a share of GDP and real GDP per capita in both groups of countries over the 40 years. The relationship is similar for individual countries (figure 3.2). Botswana and Nigeria are interesting outliers. Both are richly endowed with extractives (diamonds in Botswana and crude oil in Nigeria), which have substantially raised the share of exports in their economies. But while Botswana managed to raise its GDP per capita significantly over the 40 years, Nigeria barely moved it. Part of the reason is Nigeria’s much larger population (169 million versus 2 million in 2012). But part must also stem from differences in policies and institutions.\(^2\)

**The East Asian model and its relevance to Sub-Saharan Africa**

The East (and South-East) Asian countries pursued, with some variations, an export promotion model that had many common elements—and served them well. The general thrust of the model could still be useful for Sub-Saharan countries, if adapted to reflect changes in global trading rules, sources of demand growth, and sources of comparative advantage. It would also have to suit the circumstances of individual countries.

**Outlines of the East Asian export strategy**

East Asian countries started with labor-intensive exports—such as textiles, food, beverages, toys, wigs, and the assembly of simple industrial products that took advantage of their relative abundance of labor and low wages. And increasing access to education, initially at a basic level, ensured that the labor force was trainable for work in industry. Over time they steadily raised the skills of their labor forces by expanding access to secondary and higher education. They made sure that the training offered by the education system was aligned to their economic development needs by paying particular attention to technical and vocational education (chapter 4).

The countries built on their advantage in cheap and productive labor with policies, incentives, and institutions that favored exports—and in many cases restricted imports. They maintained stable macroeconomic environments and ensured (through periodic devaluations) that their exchange rates did not make their main exports uncompetitive. And with the possible exception of Hong Kong SAR (China) and Singapore, they used tariffs and other measures to protect domestic...
import-substitution industries. But they did not shelter them behind protective walls for long, as happened in Sub-Saharan Africa. Protection was often granted to firms against performance requirements that usually included being able to export. And the state helped firms improve their production capabilities and their ability to export. The export promotion instruments ranged from the general (or horizontal)—in principle available to every firm in the economy or in a set of identified sectors—to the very specific (or vertical)—tailored to particular firms or products (box 3.1).

Malaysia, Singapore, and Thailand focused on attracting foreign direct investment (FDI), and Japan and South Korea on grooming homegrown “champions”—private conglomerates that initially used mostly licensing to acquire foreign technology. Taiwan (China) and later China pursued a mixed strategy involving large state-owned enterprises, small private domestic companies, and foreign firms. Almost all of them used special economic zones or specialized industrial parks that provided upgraded infrastructure and streamlined procedures as well as fiscal and trade policy incentives to attract export-oriented FDI and domestic industrial investment. Over time the special economic zones and specialized industrial parks evolved into clusters that provided the advantages of agglomeration.

With expanding import demand from the United States and Western Europe, and the relative ease of entering these markets, thanks in part to the Cold War, each of the East and South-East Asian countries rapidly expanded and gradually upgraded exports.3

Changes in the global economy

The global economy has changed greatly since the East Asian export drives started 40−50 years ago. First, there is considerable uncertainty about whether robust demand growth in the United States and Western Europe can be counted on in the future. Second, the entry of China into the world trading system, with its large labor supply, scale economies, deep domestic supply chains in industrial clusters, and excellent logistics, has raised the bar for all other countries trying to compete on global export markets on the basis of low wages.4 Third, with the advent of the World Trade Organization (WTO) in 1995, the scope for active export-promotion instruments has narrowed, so some of the instruments used by East Asia may no longer be options.

Toward a viable export-oriented strategy

What types of products and services could power exports from Sub-Saharan countries, and where will the export markets be?

Which exports?

In the short to medium term the pathways to export expansion are determined by the relative comparative advantages and disadvantages of African countries, though these can be changed over time. Broadly speaking, Africa’s existing relative advantages are abundant low-wage labor and abundant land and natural resources. By 2050 almost a fifth of the global population of working age will be in Africa. Half the world’s acreage of cultivable land not yet cultivated is in Africa. And Africa’s known reserves of oil, gas, and minerals, with further exploration over the next decades, are set to grow dramatically. However, Sub-Saharan countries are

Box 3.1 Instruments East Asian countries used to promote exports

- Access to imported inputs at duty-free prices.
- Access to import licenses and foreign exchange for imports (where these were rationed).
- Access to long-term loans.
- Automatic access to loans for working capital.
- Subsidized interest rates on loans.
- Tax exemptions and reductions.
- Facilitation of access to foreign technology through licensing, support for research and development, financial incentives to firms, or government research institutes.
- Government procurement.
- Export market intelligence.
- Export finance facilities and export credit guarantees.
- Special economic zones or specialized industrial parks.
- Public recognition for high-performing exporters (especially Korea).
Sub-Saharan countries need to address their relative cost disadvantages, particularly with China and other Asian countries at a relative disadvantage in capital (including physical infrastructure), technology, and skills. So it makes sense for them to leverage their current comparative advantage while upgrading their capabilities in the disadvantaged areas.

**Labor-intensive manufactures.** Sub-Saharan Africa’s abundant labor and low wages make it potentially competitive in the export of labor-intensive manufactures, such as garments and assembling consumer electronics (chapter 5). But since labor productivity in the region is low relative to China and other East Asian countries, abundant low-wage labor does not necessarily translate to low labor costs in production. Consider Ethiopia and Tanzania. Wages for producing polo shirts, leather loafers, and wooden chairs range from about a tenth to half those in China. But polo shirt workers in Ethiopia and Tanzania would finish half the number of shirts that workers do in China, eroding half the wage advantage (table 3.1). For wooden chairs they would produce 1 or 2 for every 100 in China, pushing Tanzania’s costs to 19 times those in China—and Ethiopia’s to 26 times. Only for leather loafers are the unit labor costs lower.5

Furthermore, poor infrastructure, onerous regulations, and official corruption tend to raise the cost of operations in Sub-Saharan Africa, so low wages do not necessarily translate to a comparative cost advantage (box 3.2).

To leverage their abundant labor resources into a competitive advantage in labor-intensive manufacturing exports (such as garments and component assembly), Sub-Saharan countries need to address their relative cost disadvantages, particularly with China and other Asian countries. One possible measure in the short to medium term, in addition to improving the overall business environment, is having well run special economic zones and specialized industrial parks to reduce the high costs from

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Source: Constructed using data from Dinh and others (2012).

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**Box 3.2 Indirect costs in Sub-Saharan Africa—the burden of operating in difficult business environments**

In addition to the direct costs of capital, labor, and raw materials, the difficult business environment in many Sub-Saharan countries, marked by poor infrastructure and governance, imposes additional costs on firms compared with those operating elsewhere.

A study based on the World Bank’s Enterprise Survey data reports that in Kenya about 70% of firms own their own electricity generators, and in Nigeria about 40% of the electricity comes from private generators. In Mozambique, Benin, Burkina Faso, Senegal, the Gambia, Madagascar, and Niger firms spend more than 10% of their total costs on energy, compared with only about 3% in China. Transport is also a major constraint on firms.

Beyond the infrastructure constraints are also other indirect costs such as licensing fees and bribes, which raise the costs of firms in Sub-Saharan Africa. Whereas in China indirect costs, which in addition to power and transport costs are defined to also include license fees and bribes, make up 5–25% of gross total value added (sales minus the cost of raw materials); in Kenya, Tanzania, and Zambia they made up 40–70%.

Source: Adapted from Ramachandran, Gelb, and Shah (2009).
poor infrastructure and onerous regulation (chapter 2). A second is targeting industry-aligned training programs at unemployed secondary and tertiary school leavers to provide low-wage labor at skill levels that are a little higher than they now are in Sub-Saharan countries, and possibly even higher than the average levels currently typical of assembly plant workers in Asia (chapter 4). A third is combating official corruption. Such measures could position Sub-Saharan countries to benefit from the rising wages in China and other Asian countries, which are pushing some exporters to relocate to lower cost areas.6

But staying competitive in the export of labor-intensive manufactures based on a low-wage advantage will become more difficult. Re-shoring and near-shoring, multinational companies from developed countries are relocating manufacturing back to, or near, their home bases. And such technological developments as three-dimensional printing and packaging of integrated circuits are likely to reduce the demand for low-skilled assembly workers.7

**Processing natural resources (and agricultural commodities).** The prospects of Sub-Saharan countries are brighter for manufacturing exports based on processing agricultural and extractive resources (oil, gas, and minerals), which they have in relative abundance. Many development successes have begun by working and transforming local natural resources.8

But processing tends to be intensive in capital and skills, so it would demand more of the factors Sub-Saharan countries lack and less of the untrained labor they have in abundance. These constraints can be overcome through skills development (chapter 4) and with deliberate programs to develop capabilities in more labor-intensive industries upstream and downstream (chapters 6 and 7).9 In agricultural processing, developing links to smallholders and improving their productivity and access to markets will also reduce rural poverty, as with oil palm in Malaysia.10

Some Sub-Saharan countries also have good export prospects in services, particularly tourism, based on the attractions of their varied cultures, exotic wildlife, and sunny beaches (chapter 8). Also possible are teleservices, such as business process outsourcing, based on fairly low wages and medium skills—for the U.K and U.S. markets for Anglophone Africa and the French market for Francophone Africa. Again, skills development, in addition to investments and policy actions, will be needed to turn potential into a competitive advantage on the global market.

A viable export-oriented strategy for Sub-Saharan countries would thus emphasize adding value to agricultural and extractive resources, developing related upstream and downstream industries, and promoting links along the chain. It would also opportunistically pursue labor-intensive manufacturing, taking advantage of FDI, and using well run special economic zones and specialized industrial parks to reduce costs. And it would promote telephone and simple information technology services and tourism based on culture and natural assets (wildlife and year-round sunny beaches). All have to be based on a higher platform of skills, so short-, medium-, and long-term strategies to develop skills have to be core parts of the export drive.

**Where are the export markets?**

The European Union, Japan, and the United States have been the traditional export markets for Sub-Saharan countries. They were also the main markets for the rising exports of East and South-East Asian countries. But these markets cannot be counted on to do the same for Sub-Saharan countries. They will continue to be very important, and Sub-Saharan countries need to continue efforts to expand their exports to them. But they also have to explore and expand their access to other markets, especially the emerging markets in Brazil, China, and India and the internal market in Africa.

The European Union is still the major market for Sub-Saharan exports (figure 3.3). But China has eclipsed the United States, with India following as the third largest (table 3.2). China, India, and Brazil lead in market growth (figure 3.4). Note that intra-Sub-Saharan exports, though small, have grown faster than exports to the European Union and the United States—from around 9% in 1990 to almost 12% in 2012.

**Markets in OECD countries.** Sub-Saharan countries should still strive to expand their exports to the European Union and the United States. They should seek to take better advantage of preferences available to them, but in ways that do not foreclose their policy options for diversifying their production and upgrading their technologies. With the end of the Multi Fibre Arrangement and the arrival of the WTO in 1995, the United States in 2000 offered trade preferences (duty-free and quota-free access, subject to certain limitations) to eligible Sub-Saharan countries under the African Growth and Opportunities Act (AGOA). And the European Union offered Everything But Arms (EBA) to the 49 least developed countries, 27 of them in Africa, and Economic Partnership Agreements (EPAs) to many others.11

Although helpful, AGOA and EBA have serious limitations, including...
country coverage, product coverage, rules of origin, and uncertainty about their duration. AGOA sets stringent performance-based criteria for eligibility, while the EBA’s primarily income-based criterion excludes many Sub-Saharan countries that have good prospects for trade (such as Ghana and Kenya). And since the least developed, developing, and middle-income countries of Sub-Saharan Africa tend to belong to the same regional economic groupings, EBA’s and particularly the EPAs’ distinctions among these countries complicate efforts to create regional markets.

Coupled with rules of origin, the distinctions could discourage the least developed Sub-Saharan countries from procuring inputs from other Sub-Saharan countries. Similarly, the reciprocity requirement of EPAs could discourage regional economic groups in Sub-Saharan Africa from moving to common external tariffs to enlarge regional markets.

Product coverage of the preference schemes is sometimes a problem as well. At more than 90% the product coverage of AGOA appears high, but the reality is that many countries produce and export only a narrow range of products, so the few tariff lines excluded from the preferences could make a huge difference to them. For example, AGOA excludes cotton and other agricultural commodities that loom large in the exports of several African countries. Indeed, 90% of Sub-Saharan exports under AGOA are petroleum.

The rules of origin for the programs are different and tend to be complicated, especially for EBA, making it difficult for Sub-Saharan exporters to benefit. And the rules of origin specified in percentages of value added do not reflect the reality of today’s fragmented task-based production and exports in global value chains. Setting the required local value-added percentage high...
China’s growth and rising incomes also present African countries with market opportunities as well as challenges. It makes it very difficult for countries to take advantage of the task-based production in global value chains to promote exports.

Moreover, uncertainty over whether each round of AGOA (and some of the other trade preferences) will be renewed on expiration further reduces the incentives of businesses to make large long-term investments to take advantage of them.

While African countries do their part to make better use of these preferences, the United States and the European Union also need to reform them to better serve the aspirations of Africans for economic transformation (box 3.3).

Markets in the emerging economies (China, India, and Brazil). China’s rise as a global trading power has squeezed Sub-Saharan countries’ ability to compete in manufacturing exports. But its growth and rising incomes also present African countries with market opportunities. The same applies to the expanding economies of India and Brazil.

The expanding Chinese market also carries some risk. A large part of China’s demand from Sub-Saharan countries is for raw natural resources (figure 3.5). The high demand for natural resources by China to power its explosive growth has pushed up world commodity prices. This is good for Sub-Saharan countries in the short term, as it raises incomes and foreign exchange earnings. But...
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Promoting exports—essential for transformation

Africa is expanding with the growth of the middle class and urbanization for Sub-Saharan countries within the middle class export market. The potential of regional trade. Markets in Africa—the rising middle class and the potential of regional trade. The potential export market for Sub-Saharan countries within Africa is expanding with the growth of the middle class and urbanization. The African Development Bank estimates that in 2010 the size of the middle class in Africa (not just Sub-Saharan Africa) was 327 million, or 34% of the population, having grown from 26% in 1980. So far, the growth of the middle class in most countries has been fueled mainly by growth in services—finance, telecommunications, and donor-financed activities, including foreign-financed nongovernmental organizations. For its growth to continue, manufacturing activities will have to create more job opportunities for middle class incomes, which in turn will generate growing demand for manufactured consumer goods, processed and convenience foods, and high-value services.

With borders in the region more open, African countries could capture these opportunities through intraregional trade, advancing their economic transformations. Otherwise, most of the demand growth would leak to imports from outside the region, which could slow the pace of transformation. So, African policymakers need to take a more serious approach to implementing the various regional agreements on regional free trade, customs unions, and economic integration. The larger integrated regional markets would also make countries in the region more attractive for large manufacturing plants of foreign and domestic investors.

Key differences between the proposed Sub-Saharan strategy and that of East Asia. While taking advantage of low labor costs, this strategy puts more emphasis on leveraging Sub-Saharan Africa’s relative advantages in abundant natural resources. The skills required would also be a little higher than those generally prevailing in the South-East Asian countries when they initiated their export drives in the 1960s and 1970s. The strategy is also a little different in the markets to target—emerging and African countries as well as OECD markets. In addition, the promotional instruments the state could use to implement the strategy would have to be modified in some key respects.

Promoting exports—how

Formulate an explicit export promotion strategy

If countries see expanding and diversifying exports as top priorities, they need clear strategies for pursuing them. An export promotion strategy could be an elaboration of the objectives for exports in the National Transformation Strategy (chapter 2). Among the key areas to address in the export promotion strategy:

- Maintaining a general economic environment that makes exporting profitable.
- Adding value to selected traditional exports, based on market prospects.
- Providing targeted support to promising nontraditional or new exports, including technologically more advanced exports.
- Strengthening the country’s position in existing export markets and diversifying into new ones.
- Attracting export-oriented FDI, particularly in manufacturing.
- Responding to the immediate skill requirements of the exports being promoted.

Indeed, since export promotion is such a key part of overall economic transformation, the discussion here in many ways mirrors that in chapter 2 on promoting overall transformation, looked at through an exports lens.

Export promotion requires a whole-government approach and close state–private sector collaboration. As with the overall economic transformation strategy, the export strategy should be developed in consultation with the private sector. And it should have sensible targets discussed and monitored by the state and exporters in the state–private sector collaboration forum. Export promotion requires more than just the Ministry of Trade.
and Industry and the Export Promotion Agency. It requires several ministries and agencies in government, including the Ministries of Planning, Finance, Agriculture, Infrastructure, Education, Science and Technology, Mineral and Petroleum Resources, Tourism—as well as the Central Bank and the Export Credit and Guarantee Agency. Coordination within government by a central coordinating agency is thus essential.

Enhancing the profitability of exports. A realistic exchange rate policy is key to the profitability of exports because it determines how much exporters receive in domestic currency for their foreign exchange earnings. If the exchange rate is too low, receipts in domestic currency for their foreign exchange earnings. If the exchange rate is too low, receipts in domestic currency cannot cover their costs, and they cannot survive as exporters.17 To avoid this, the exchange rate should, at a minimum, move over time to reflect movements in the costs of domestic factors of production once it has been set initially at a level that makes a significant number of exports profitable.18

Since the exchange rate also determines the domestic currency price of imports and therefore the welfare of a large number of consumers and producers, the government cannot just keep hiking it to keep up with rising domestic costs. It will be important, therefore, to take measures to contain domestic costs.

Prudent macroeconomic policy that controls inflation can keep domestic costs down. Efficient administration of customs and ports can also save exporters unnecessary costs and delays. Domestic exporters are put at serious cost disadvantage if they have to pay high tariffs on imports used in producing exports. But a duty drawback or bonded warehouse scheme can ensure that they get access to imported inputs at free-trade prices. They are similarly disadvantaged if they do not have access to reliable infrastructure at reasonable prices. In the short term special economic zones can provide quality infrastructure (which the country cannot afford to provide on a national basis), ease the administration of duty drawback schemes, and pilot the streamlining of regulations.

Export credit and insurance are also critical, and several governments run programs to cater to these needs, including guarantees to banks to ease exporters’ access to credit (box 3.4). But such incentives are sometimes considered subsidies and may thus be subject to countervailing duties.

Apart from these general measures, governments may also find it

**Box 3.4 Financing exporters’ working capital with cascading letters of credit**

One of the biggest things exporters need is automatic access to working capital to cover their operating costs from the time they receive an export order to the time they receive payment.

In developed markets exporters can get credit from banks against an export letter of credit. The Korean central bank, Bank of Korea, took this a step further with cascading domestic letters of credit to an exporter’s suppliers and to the suppliers of those suppliers, all the way to small shops in the mountains. (Korea was proud to have invented the system, but it turns out Japan used a similar system in the 1950s, as did England in the 1800s.)

This may sound straightforward, but there are some wrinkles, and the administrative arrangements are crucial in running the system.

Exporters might use the working capital loans to produce for the home market, so the loans have to be tied to what is needed for export. That requires documentation of the order, of the cost of inputs needed to fulfill the order, and of the completed order. The same is true for suppliers, so coefficients are needed for the part of their production that will eventually be exported, and setting those coefficients is not a simple administrative order. Given their data and capacity constraints, African countries will have to exploit simpler ways of implementing such a system.

The innovation was to extend domestic letters of credit to local suppliers. That draws them into value chains and producing inputs that meet global standards.

It works only if exporters and their suppliers have duty-free access to imported inputs, an essential complement. Exporters pay tariffs and indirect taxes when they import their inputs and draw back the rebates when they document the completed export—still quite a burden. But early on they received rebates on the basis of export orders and did not have to wait.

A big part of export diversification requires learning and technological upgrading, areas where the market often fails, opening the door to productive state-business collaboration.


Justifiable to use fiscal or credit measures to enhance the profitability or reduce the production and marketing costs of selected export products or selected types of firms, such as domestic small and medium-size enterprises or export-oriented foreign-owned subsidiaries, subject to compliance with WTO rules.

Diversifying exports. Diversifying export products and services requires upgrading existing exports (such as processing traditional agricultural commodity exports) or entering new exports, which often requires higher technology. A big part of export diversification thus requires learning and technological upgrading, areas where the market often fails, opening the door to productive state-business collaboration. (Chapters 5–8 provide examples of such opportunities and how countries can respond to the challenges.)

Deepening and diversifying export markets. Governments should provide exporters with good and timely information on export markets. They can start by having their ministries of trade and industry, in consultation with exporter associations, assign well-trained economists and business school graduates to key embassies abroad. They can also consider full commercial sections abroad, either as sections in the embassies or as separate offices, preferably overseen and run mainly by exporters, with some personnel and financial support from government. Taiwan’s (China) External Trade Development Council has been very effective in providing information, organizing participation in trade fairs, and carrying out market research, with a majority of council members from industry and export associations. Started in 1970 and financed by a 0.0625% levy on exports, it had 42 overseas offices by 1983. Another example is the Korea Trade Promotion Council. Governments could also consider subsidizing carefully designed external trade promotion tours by exporters, as Mauritius does.

Active export promotion under the World Trade Organization

The WTO has reduced the scope for active export promotion, banning or severely circumscribing some instruments that the East and South-East Asian countries used from the 1960s to the 1990s. The policy space is now much narrower than in the pre-WTO era when today’s developed countries were transforming their economies or when the East Asian countries were pushing exports. But Sub-Saharan countries, particularly those temporarily exempted from the subsidy prohibition, still have some room to actively promote exports. In addition to making smart, aggressive, and efficient use of the exemptions, they can also come up with other efficient and WTO-compatible ways of promoting exports.

Protecting domestic producers

Import substitution has often been the gateway to breaking into export markets. The significant share of unbound tariffs and the gap still prevailing between bound and actual tariff rates for many Sub-Saharan countries, together with the more favorable safeguard provision on imports, still provides room for selective import substitution. In some sense, the cap on bound rates can be seen in a positive light. It rules out excessively high tariff rates that foster highly inefficient import-substitution industries. It also strengthens the hand of policymakers in resisting pressure from domestic industry for high levels of protection.

Import-substituting firms benefitting from import protection could be required to become internationally competitive (with exports or with imports on the domestic market) within a specified period. This could be done by making it explicit, when increasing a tariff, that the raised tariff will last only up to a specified date—or that an existing high (applied) tariff rate will be reduced by a certain date.

Providing subsidies to promote exports

A deficiency in tariff protection is that even if the raised rates are explicitly temporary, there is no way to discipline firms enjoying the protection if they fail to improve their efficiency. Subsidies can overcome this disadvantage since the actual payment or conferring of the benefits can be firm-specific and contingent on performance even if the eligibility criteria are objective and broad. Subsidies that have been used by countries to promote exports include cash payments, credit at below market interest rates, tax exemptions, reduced tax rates, and reduced prices for services such as infrastructure. And making the subsidies contingent on exports provides a practical and efficient way to monitor and enforce discipline. To be considered, however, are the opportunity costs in relation to other government spending, given the other urgent needs in poor countries.

Most Sub-Saharan countries are now exempt from the WTO prohibition on using subsidies that are specific to and contingent on exports. This enables them to use export processing zones or special economic zones to attract firms, particularly foreign-owned firms, and to encourage them to export. But countries should view subsidies contingent on exports as temporary measures to facilitate building domestic capability and productivity. The quicker these are built and the subsidies withdrawn, the better.
There is no merit in a poor country persisting in paying subsidies to supply goods and services to other countries, particularly richer ones, at lower prices.

The trend under the WTO is toward stricter controls on specific subsidies contingent on exports, so Sub-Saharan countries need to come up with other approaches. Subsidies could be targeted at firms and made contingent on producing specified products at no higher than prescribed unit costs. The unit cost could be benchmarked against those of successful developing-country exporters of the products in question. This is equivalent to requiring subsidy recipients to be internationally competitive. Implementing such a system takes more than simply requiring firms to export, but the requirement focuses more directly on the root problem, which is operational efficiency and cost reduction, and it applies equally to import substitution and export promotion.

The greater complexity in this approach is one more reason to build higher skills in key agencies (such as those for investment and export promotion) and to increase collaboration between the state and the business community. Since cost reduction requires action by firms and by the state (such as reliable and reasonably priced infrastructure, and streamlined regulations), subsidies contingent on cost reduction could be part of a concrete program for public-private dialogue and collaboration to promote economic transformation.

Requiring firms to hire local workers

The Agreement on Trade-Related Investment Measures prohibits governments from requiring firms to buy "products of domestic origin." But it places no restrictions on the requirement for firms to hire local labor, which in principle could apply to both foreign and domestically owned firms (and thereby satisfy the national treatment requirement). However, such a requirement must be consistent with the profit motives of firms, and the country must have people with skills that firms, including foreign firms, would find in their economic interest to hire. So, there is still scope for countries to combine focused skills development with strategic programs to attract export-oriented foreign-owned firms. Highly trained locals that foreign-owned firms find economical to take on as managers, engineers, and technicians not only provide employment. They also present a cadre of potential entrepreneurs who could set up dynamic modern firms in the future, as in Ireland, Malaysia (Penang), and Singapore.

Increasing access to technology

The Agreement on Trade-Related Aspects of Intellectual Property Rights now makes it more difficult for firms to acquire technology through copying, reverse engineering, or lax enforcement of copyright and patent laws—methods the developed countries and successful East Asians used in the past. There is an expectation in the agreement that developed countries would make it easier for less developed countries to access technology, but it is not clear how this would be implemented, monitored, or enforced.

Governments have two main options to help their firms acquire technology. First, they can facilitate licensing by providing access to information (including subsidized technology study tours), easing regulations, and providing targeted subsidies, contingent on performance, to lower the cost of technology licenses (or critical new machinery). Second, they can establish R&D facilities that address technological constraints in specific subsectors in consultation with firms (see box 2.9 in chapter 2).

So, although the WTO regime now restrains active export promotion measures, Sub-Saharan governments, particularly those in the developing and least developed countries, still have room to maneuver—if they are creative.

* * *

Expanding, diversifying, and technologically upgrading exports have to be part of the economic transformation agenda. Given the current international trading environment and the relative endowments of Sub-Saharan countries, the export-oriented strategies and the instruments for their pursuit will have to differ from those the East and South-East Asian countries used successfully from the 1960s to the 1990s.

Although the region has low wages and a growing labor force, these do not always translate into competitive advantage on labor costs because of labor's low productivity. Aggressive skills development and training will thus be needed for the region to leverage its potential comparative advantage in abundant low-wage labor. Streamlined regulations and improved infrastructure (possibly in special economic zones and specialized industrial parks in the short term) will also help reduce costs. But governments will have to supplement them with more focused efforts at export promotion. This will include macroeconomic, exchange rate, and other horizontal measures. But also needed are vertical efforts to promote targeted exports, which may entail performance-based subsidies and other support to exporters to help them acquire and master technology, develop new exports, and expand into new markets. Although the WTO regime puts...
some restraints on the proactive export promotion measures, for the developing and least developed countries of Sub-Saharan Africa there are still options that governments could use creatively.

A reasonable export strategy for countries in the region would leverage their relative comparative advantage in agriculture and natural resources and take advantage of their low-wage labor. Prospective world demand suggests that while the traditional markets of the European Union, Japan, and the United States will continue to be important, Sub-Saharan countries should also expand their exports to such emerging economies such as Brazil, China, and India. But they need to avoid being lured by high commodity demand into relaxing their efforts to industrialize and upgrade the technology of their exports. The regional market in Sub-Saharan Africa could also support a dynamic expansion of exports, but governments will have to do much more to remove barriers to intraregional trade and to improve regional transport infrastructure.

Notes

1. Although cross-country regression studies between economic growth and exports appear inconclusive, case studies of the East Asian countries clearly show the decisive role of exports in their GDP growth and economic transformation in general. See World Bank (1993), Lall (1997, 2004), Pangestu (2002), and Weiss (2005).

2. See, for example, Acemoglu, Johnson, and Robinson (2003).


4. The rise of China as a global economic and trading power also presents some potential opportunities discussed later in the chapter.

5. Dinh and others 2012.

6. Average monthly wages in manufacturing in urban areas increased by an average of 14.2% a year from 2003 to 2011 (in nominal yuan). In nominal U.S. dollar terms it increased 17.9% a year over the same period. For wage rates in yuan see (National Bureau of Statistics of China 2011); for exchange rates see International Monetary Fund elibrary, accessed July 10, 2013.


8. Examples include Britain at the start of the industrial revolution (iron and coal); similarly for Belgium, France, Germany, and the United States (which was a leading producer of several minerals and also petroleum). Other examples include Finland and Sweden (forestry products).

9. For example, Finland and Sweden leveraged forestry resources into increasingly sophisticated products, including production of the associated machinery and engineering services (Blomstrom and Kokko 2007). The mining engineering expertise of the United States in the nineteenth century, or more recently of Australia and even South Africa are other relevant examples (Wright and Czelusta 2007). Chile (salmon, wine, and fruits) and Malaysia (palm oil) have been able to leverage their potential in agriculture into global comparative advantage. (Both examples in Chandra [2006].)


11. Other OECD countries such as Canada also have trade preferences for developing countries that cover Sub-Saharan countries.


16. The African Development Bank defines the middle class in Africa as those with per capita daily consumption level of $2–20 in 2005 PPP terms. This group is classified into three categories: the floating class, with daily per capita consumption of $2–4; the lower middle class, with consumption of $4–10 a day; and the upper middle class, with daily consumption of $10–20. Of the estimated middle class population in Africa in 2010 of 326.7 million, 61% was in the floating category, 25.5% in the lower middle class, and 13.5% was in the upper middle class (AFDB 2011).

17. The exchange rate is defined for this discussion as the units of domestic currency per a unit of foreign currency. Currencies of major or potentially major trading partners are particularly important. In fact it may be important for policymakers to also track the effective exchange rate, which is the units of domestic currency for a weighted unit of the currencies of main trading partners.

18. In other words, the real exchange rate should be stable over time once it has been set at an appropriate initial level. This is a minimal condition in the sense that changes in external markets (such as emergence of external competitors with much lower costs and prices) may necessitate additional movement in the exchange rate.


22. For instance, see World Bank (1993).


24. For example, Correa (2005).

25. Subsidized study tours have been an important source of learning about technology for Chilean producers and exporters of salmon and wines (Katz 2006; Benavente 2006).

References

World Development Indicators (database). World Bank. Washington, DC.